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In the Supreme Court of the United States

OCTOBER TERM, 1980

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.,
PETITIONER,

VS.

J. J. CURRAN AND JACQUELYN L. CURRAN,
RESPONDENTS.

On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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REPLY BRIEF OF PETITIONER, MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.

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I.

A HOLDING BY THIS COURT THAT NO PRIVATE RIGHT OF ACTION EXISTS UNDER SECTION 4b OF THE CEA WILL NOT LEAVE RESPONDENTS WITHOUT A REMEDY.

The Currans argue that the CEA reparations procedures were unavailable to them and that consequently they had no remedy in the absence of an implied right of action under the CEA (RB 1).[1] They base their argument on section 14(i) of the CEA[2], the thrust of which is that reparations are available only for "claims which arise" after January 23, 1975. The Currans assert that their cause of action accrued prior to May, 1974 (RB 1).

Respondents' argument must be rejected because they alleged completely different facts before the trial court and should not be allowed to submit a conveniently altered set of facts for the very first time before this Court. *Cf., Imperial Casualty & Indemnity Co. v. Relder*, 308 F.2d 761, 763 n.1 (8th Cir. 1962). Specifically, on August 20, 1976, the Currans filed a brief entitled "Plaintiff's Reply Memorandum In Opposition To Motion To Dismiss And Stay Proceedings". At pages 19-20 the Currans told the District Court that because they discovered the alleged fraud after April 5, 1975, their fraud claim by law accrued less than one year prior to the filing of the complaint on April 5, 1976 — *i.e., after* April 5, 1975. Because section 14(i) provides that reparations are

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[1] "RB__" refers to the Brief of Respondents; "PB__" to the Brief of Petitioner.

[2] CEA section 14(i), 7 U.S.C. §18(i) states: "The provisions of this section shall not become effective until 15 months after October 23, 1974: *Provided*, That claims which arise within one year immediately prior to the effective date of this section may be heard by the Commission after such fifteen months period."

available for claims arising after January 23, 1975, Respondents' contention must obviously fail.

Even assuming that the fraud claim arose prior to January 23, 1975, the Currans' statements in the District Court to the contrary notwithstanding, their assertion that they have no remedy in the absence of an implied private right of action under the CEA is incorrect. In such circumstances, and prior to the existence of the pervasive regulatory scheme embodied in the post-1974 CEA, Respondents could sue for fraud in state court under the common law of Michigan.

The Commodity Futures Trading Commission Act of 1974, P.L. 93-463, 88 Stat 1389 ("1974 Amendments"), which completely overhauled the CEA, was enacted on October 23, 1974. One major consequence of the legislation was the addition to section 2(a)(1) of the following preempting language: "...[The Commodity Futures Trading] Commission shall have exclusive jurisdiction with respect to accounts, agreements...and transactions involving contracts of sale of a commodity for future delivery..." This langauge operated to oust state courts of jurisdiction over fraud involving transactions in futures, and other conduct violative of the CEA.[3] However, the effective date of this language was April 23, 1975 — 180 days after enactment. *See* §418(a) of the 1974 Amendments at [1974] U.S. Code Cong. & Ad. News 1589, 1622. Therefore, assuming Respondents are correct and their

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[3] The CFTC, as *amicus curiae*, disputes the preemptive effect of the 1974 Amendments (CFTC Brief at 11, n.14). The issue of whether the 1974 Amendments preempt a right to pursue, in *state* court, a common law fraud claim involving futures contracts is not presented by this case and need not be addressed by the Court. To the extent the Court believes the issue is relevant, Merrill Lynch submits that the "exclusive jurisdiction" provision of CEA section 2(a)(1), 7 U.S.C. §2, together with the pervasive regulatory scheme embodied in the 1974 Amendments, plainly indicates Congress' preemptive intent.

fraud claim arose prior to January 23, 1975, this was at least three months before the preemptive 1974 Amendments deprived state courts of their jurisdiction over fraud involving futures contracts. Consequently, the Currans would not be without a remedy even if this Court were to accept their revised version of the facts. They could sue Merrill Lynch for fraud in state court under the common law.

The Currans' plea that absent an inferred federal judicial remedy they are without a forum in which to seek redress is not, therefore, persuasive. If, as the Currans claimed in the District Court, their claim accrued after April 1975, the Currans can pursue reparations under CEA section 14. If, as they now argue, their claim accrued in May 1974, they may seek redress in the state courts. Finally, it should be noted that Merrill Lynch has sought to arbitrate Respondents' claim pursuant to the agreement Respondents signed when they opened their accounts, thereby offering yet another available forum.

Regardless, however, of whether their claim accrued prior or subsequent to the effective date of the 1974 Amendments, the Currans may not bring suit against Merrill Lynch in federal court under the CEA. A few erroneous lower court decisions to the contrary notwithstanding, there has never been a private cause of action under section 4b of the CEA, neither before nor after the 1974 Amendments. Since enactment of the CEA in 1936, there has never been language in the statute providing for such right of action, and there has never been anything in the legislative history indicating any Congressional intent that such right of action exists.[4]

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[4] For a full discussion of whether an implied private right of action in federal court could properly have been recognized under the CEA prior to the 1974 Amendments, see Brief of Petitioner Clayton Brokerage Co. filed in *Clayton Brokerage Co. of St. Louis, Inc. v. Leist*, No. 80-895.

II.

PRE-1974 CASE LAW DOES NOT JUSTIFY AN INVERSION OF THIS COURT'S INQUIRY UNDER *CORT* v. *ASH*: RESPONDENTS' INVITATION TO FOCUS ON WHETHER CONGRESS MANIFESTED AN INTENT TO DENY A "PRE-EXISTING REMEDY" CONCEDES THAT SUCH A REMEDY WAS NEVER AFFIRMATIVELY CREATED.

Cort v. Ash, 422 U.S. 66, (1975), *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979), *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979) and *Middlesex County Sewerage Auth. v. National Sea Clammers Assn.*, ____ U.S. ____, 49 U.S.L.W. 4783 (June 25, 1981) require an affirmative showing that Congress intended to legislate a private right of action under CEA section 4b.[5] As demonstrated in the Brief of Petitioner, and in the Brief of Petitioner Clay-

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[5] *Amicus* CFTC purports to distinguish *National Sea Clammers*, claiming that the case puts the burden on Petitioner to show an affirmative Congressional intent to extinguish an existing remedy (Brief of *amicus* CFTC at 8, n.9). What *National Sea Clammers* actually holds, of course, is that when there is a preexisting private right of action *expressly created by statute* (in that case 42 U.S.C. §1983), the party alleging that such *express* right of action has been implicitly foreclosed by subsequent regulatory legislation has the burden of establishing that implicit intent. Here, establishing federal jurisdiction remains the Currans' burden, and since the CEA does not expressly confer the jurisdiction asserted, it is the Currans' burden to establish an affirmative Congressional intent to create the alleged right of action.

The Court's decision in *National Sea Clammers* weighs heavily against the Currans' position. In that case, enactment of a pervasive regulatory scheme was held sufficient to demonstrate Congressional intent implicitly to abrogate an *express* statutory right of action. In the case at bar, a similarly pervasive regulatory statute manifestly precludes inference of an additional remedy that Congress never affirmatively created.

ton Brokerage Co., No. 80-895 (with respect to the 1936 enactment of the CEA), since the CEA's inception in 1936 there has been nothing in its legislative history nor in the language of the statute itself indicating the existence of such actions. Respondents, and the Commodity Futures Trading Commission ("CFTC") as *amicus curiae*, have attempted to avoid the requirements of *Cort, Touche Ross, Transamerica* and *National Sea Clammers* by claiming that a private cause of action for fraud existed prior to the CEA's restructuring in 1974 due to "the unanimous interpretation of the federal courts that § 4b of the CEA afforded a private remedy for commodity futures traders against their own brokers" (RB 17-18), and by arguing that the proper inquiry therefore is whether Congress in 1974 intended to repeal the alleged preexisting private action.

The Currans' argument rests upon the false premise that the courts may legislate causes of action. Furthermore, in the process of seeking to invert the focus of *Cort, Touche Ross, Transamerica* and *National Sea Clammers*, Respondent and the CFTC have found it necessary greatly to exaggerate the scope of pre-1974 federal court decisions concerning private suits under CEA section 4b. As will be shown below, very few district courts, and not a single appellate court, found an implied right of action under section 4b prior to the 1974 amendments.

Merrill Lynch urges that the Currans' inversion of *Cort* and its progeny not distract this Court from the most important fact before it: the absence from the statute, both before and after the 1974 Amendments, of the 20 or so words necessary to create — simply, clearly and unambiguously — a private right to sue in federal court for damages arising from violation of section 4b. It is this omission which places on *Respondents* the burden of establishing an *affirmative* Congressional intent to *create* a cause of action. This omission has even greater

significance following the 1974 Amendments, when the omission persisted despite comprehensive Congressional review and expansion of the statute, including enactment of an elaborate remedial scheme providing for quasi-judicial reparations proceedings.

A brief discussion of the pre-1974 decisions cited by the Currans will show that they have not accurately characterized the state of the law prior to 1974. The assertion that it was the "unanimous interpretation of the federal courts" that private suits were permissible under CEA section 4b is greatly exaggerated.

A. Certain Decisions Cited By Respondents Did Not Deal with CEA Section 4b.

United Egg Producers v. Bauer International Corp., 311 F. Supp. 1375 (S.D.N.Y. 1970), held that the plaintiff agricultural cooperative could obtain a preliminary injunction against the defendant, an egg importer, for willfully issuing false and misleading statements in violation of CEA section 6(c). There was no customer-broker relationship before the court, and CEA section 4b was not in issue.

Deaktor v. L.D. Schreiber & Co., 479 F.2d 529 (7th Cir. 1973), held that claims by traders against the Chicago Mercantile Exchange and members thereof for alleged violations of CEA sections 5a(8) and 6(c) were not within the primary jurisdiction of the Commodity Exchange Commission. The court went on to hold that a private lawsuit could be predicated on these sections, but CEA section 4b was not in issue. Furthermore, *Deaktor* was reversed by this Court in *Chicago Mercantile Exchange v. Deaktor*, 414 U.S. 113 (1973), which held that the Commodity Exchange Commission did have primary jurisdiction. This Court did not address the private right of action issue.

Seligson v. New York Produce Exchange, 378 F. Supp. 1076 (S.D.N.Y. 1974), *affirmed on other grounds*, 550 F.2d 762 (2d Cir. 1977), *cert. den.*, 434 U.S. 823 (1977) cited the Court of Appeals decision in *Deaktor* and held that a cause of action is available to exchange "member-brokers" against an exchange, apparently referring to CEA section 5(d). Section 4b was not in issue.

B. Members of Congress Debating the 1974 Amendments Could Not Have Been Aware of Certain of the Decisions Cited by Respondents.

Seligson, *supra*, was decided on May 17, 1974, only five months before final enactment of the 1974 Amendments. Consequently, besides failing to address the CEA's antifraud provisions, *Seligson* was very possibly unknown to the legislators debating the 1974 Amendments.

Hirk v. Agri-Research Council, Inc. [1974-75] Fed. Sec. L. Rep. (CCH) ¶94,738 (N.D. Ill. 1974) held that private damage actions were permissible under section 4b, but was decided June 24, 1974, a mere 120 days prior to the enactment of the 1974 Amendments. It is very possible that none of the legislators debating the amendments were aware of this decision.

The appellate decision in *Hirk*, 561 F.2d 96 (7th Cir. 1977) devoted one sentence of a footnote to this issue, was decided more than two years after the overhaul of the CEA and obviously had no impact on the legislators' decision. The same is true of *Bartley v. P. G. Commodities Associates, Inc.* [1975-1977] Comm. Fut. L. Rep. (CCH) ¶20,123 (S.D.N.Y. 1975).

C. Certain Decisions Cited By Respondents Are Inapposite.

In *Hecht v. Harris Upham & Co.*, 283 F. Supp. 417, 437 (N.D. Cal. 1968), the District Court held that on the facts before it, which involved both securities and commodities, the "churning" of the plaintiff's commodity account could "be regarded as a mere device for churning the security account . . ." Accordingly, the court concluded that the defendant was liable for churning the plaintiff's accounts "in violation of §10b of the Securities Act . . ." 283 F. Supp. at 439-40. No mention was made of a CEA violation, and the issue of private suits under the CEA was not addressed. The Court of Appeals affirmed, modified the damage award and said nothing about private causes of action under the CEA. 430 F.2d 1202 (9th Cir. 1970).

The District Court in *Gould v. Barnes Brokerage*, 345 F. Supp. 294 (N.D. Tex. 1972), with no reasoning or case support whatsoever, stated that it had jurisdiction over claims based on the CEA by virtue of 28 U.S.C. §1337. The court did not address the substantive issue of whether a private cause of action existed for violation of the CEA.

In *Johnson v. Arthur Espey, Shearson, Hammill & Co.*, 341 F. Supp. 764 (S.D.N.Y. 1972), the plaintiff was a stockholder suing derivatively on behalf of a corporation for alleged churning of a corporate commodity account. Although the court opined that the complaint stated a claim under CEA section 4b, it dismissed the plaintiff's claims without prejudice for failure to make demand for redress upon the corporate directors prior to filing suit.

In *Booth v. Peavey Co. Commodity Services*, 430 F.2d 132 (8th Cir. 1970), the Court of Appeals affirmed a directed verdict for the defendant that there was no churning of the plaintiff's commodity account. The court stated its belief that a

private action under the CEA for churning is permitted, but only after the court acknowledged that "the point has not been argued by the parties. . ." 430 F.2d at 133. This observation was not at all necessary to the decision because the court affirmed the trial court's decision that there was, on the basis of the facts before it, no churning of plaintiff's account. As unsolicited dictum, this facet of the opinion carries little weight.

Respondents therefore are left with only four district court cases to support their contention that "it was the unanimous interpretation of the federal courts" that section 4b provided a private remedy (RB 17).

D. Respondents' Four Pre-Amendment District Court Decisions Did Not Create a Private Cause of Action Under CEA Section 4b.

The four district court cases upon which the Currans rely to establish their claimed right of action are: *Goodman v. Hentz*, 265 F. Supp. 440 (N.D. Ill. 1967); *Anderson v. Francis I. du Pont & Co.*, 291 F. Supp. 705 (D. Minn. 1968); *McCurnin v. Kohlmeyer & Co.*, 340 F. Supp. 1338 (E.D. La. 1972); *Arnold v. Bache & Co., Inc.*, 377 F. Supp. 61 (M.D. Pa. 1973). *Goodman* is the most important of these decisions. It was the first to so hold, and is the decision which all the other cases cite, sometimes verbatim and at length. It therefore merits special attention.

Goodman was decided 31 years after enactment of section 4b, and characterized the issue under discussion as a "novel question". 265 F. Supp. at 446. The court based its decision on the law of negligence as set forth at Restatement, Torts, §286, and stated that:

> Violation of a legislative enactment by doing a prohibited act makes the actor liable for an invasion of the interest of another if: (1) the intent of the enactment is exclusively

> or in part to protect the interest of the other as an individual; and (2) the interest invaded is one which the enactment is intended to protect. 265 F. Supp. at 447.

This is the tort per se reasoning expressly rejected by this Court in *Touche Ross*, 422 U.S. at 568.

Respondents are asking this Court to do four things: Ignore the rules of statutory construction set forth in *Cort*, *Touche Ross*, *Transamerica* and *National Sea Clammers*; ignore Congress' purposeful omission, since the CEA's inception, of language bestowing a private right of action; ignore the glaring omission of a private cause of action from the massive remedial scheme enacted in October, 1974; and unconstitutionally legislate a private cause of action for fraud because four United States district courts did so by means of an expansive reading of the law of negligence. Only Congress — and not the district courts of Illinois, Minnesota, Louisiana or Pennsylvania — may enact legislation.

Goodman was decided only seven years prior to the comprehensive overhaul of the CEA in 1974. By way of contrast, in recognizing an implied cause of action under section 10b of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), in *Superintendent of Insurance v. Bankers Life and Casualty Company*, 404 U.S. 6 (1971), this Court "...explicitly acquiesced in the 25 year-old acceptance by the lower federal courts of a Rule 10b-5 cause of action." *Cannon v. University of Chicago*, 441 U.S. 677, 690-93 n.13 (1979). Indeed, this Court in *Bankers Life* followed literally *hundreds*[6] of lower court decisions holding in favor of implied actions under section 10b. The paucity of judicial treatment of the CEA, by way of comparison, is quite obvious. In these circumstances, it would be an infringement upon a purely legislative prerogative for the courts to engraft a private cause of action onto the CEA.

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[6] *See, Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 731 (1975).

Reliance by Respondents and *amici* upon the few pre-1974 district court cases, in conjunction with the proviso to CEA section 2(a)(1), as an expression of legislative intent to preserve a "preexisting" private right of action is misplaced. In addition to the fact that the proviso was expressly intended to serve other purposes (i.e., preservation of court jurisdiction over some contract and antitrust matters [PB 30-32]), its language does not support Respondents' theory.

Specifically, the proviso states that "[n]othing in this section shall supersede or limit the jurisdiction *conferred* on courts of the United States or any State" (emphasis added). Under articles I and III of the Constitution, only Congress can *confer* jurisdiction on the federal courts. The courts cannot confer jurisdiction upon themselves. No provision of the CEA, either prior to or after the 1974 Amendments, confers jurisdiction upon the federal courts to entertain private damage claims based upon fraud. The federal jurisdiction that the proviso preserves is that which has previously been *conferred* upon the courts in accordance with the Constitution, e.g. as in some contract (where diversity exists) and antitrust cases. It is a solecism and a boot-strap argument to claim that the proviso preserves jurisdiction that some courts have unconstitutionally conferred upon themselves through reliance upon an impermissible tort per se analysis. *See, e.g., Goodman v. Hentz, supra.*

The invitation of the Currans and *amici* to invert the analysis of *Cort* and *Transamerica*, and search for a Congressional intent to *deny* a right of action is an invitation to the courts and Congress to reverse their constitutional roles. Under Respondents' theory, the federal courts are free to define the scope of their own jurisdiction, and such jurisdiction is per se permissible unless and until Congress affirmatively acts to take it away. This might or might not be a workable theory of government, but it is not the one provided for in articles I and III of the Constitution.

To attach any importance, therefore, to the four pre-1974 decisions is to misinterpret the role of Congress in our constitutional system. A private cause of action under the CEA may be created only by a positive legislative act, not by silent acquiescence to judicial opinions. Congress has not at any time during the 45 year history of the CEA affirmatively acted to create either an express or an implicit private right of action in federal court based upon violation of the antifraud provisions of the statute.

III.

THIS COURT MAY NOT LEGISLATE A PRIVATE CAUSE OF ACTION UNDER SECTION 4b MERELY TO ENABLE COURTS TO ADJUDICATE BREACH OF CONTRACT AND FRAUD CLAIMS IN ONE PROCEEDING.

The CFTC and Samuel Friedman, in briefs filed by each as *amicus curiae*, have advanced the curious argument that this Court should recognize a private cause of action under section 4b to avoid what they perceive as an illogical fragmentation of federal court litigation. They suggest scenarios in which, for example, a futures commission merchant sues a customer in court for an account deficit, provoking a counterclaim by the customer for fraud. They conclude that if this Court holds that there is no private cause of action for fraud, the customer would have to bring his fraud claim in a reparations complaint before the CFTC, while the broker's claim would remain in court.

The procedural difficulties that *amici* claim result from this situation are more imagined than real. *Amici* ignore, for example, CFTC Reg. §12.23(b)(2), 17 C.F.R. §12.23(b)(2), which permits a broker to claim the account deficit by way of

counterclaim in reparation proceedings.[7] Sharing *amici's* interest in adjudicating all issues in a single proceeding, the broker in *amici's* scenario would, Merrill Lynch submits, typically stay or dismiss its court claim and join issues, by counterclaim, in the customer's reparation hearing. Even if *amici* are correct in alleging that some procedural inconvenience might occur, the situation, if perceived as a problem, is one that admits of legislative, not judicial, solution.

If the CEA offers the potential for parallel adjudication of broker breach of contract claims and customer fraud claims in separate forums, this result is entirely consistent with the Congressional policy manifest in the CEA. A customer who fails to pay his broker contractually agreed upon sums has not violated the CEA. He has of course breached his contract, but no provision of the CEA prohibits this particular conduct. The CEA concerns itself primarily with behavior perceived as a threat to the specialized workings of the futures markets: Willful misrepresentation, price manipulation, "cornering" of markets and excessive speculation. It does not concern itself with behavior actionable under ordinary commercial law principles, such as a failure to deliver commodities contracted for, or the failure by a customer to pay sums owing his broker.

Given the specialized concerns of the CEA, and its lack of concern with basic commercial law principles, the adjudication of a breach of contract claim in court in conjunction with specialized CFTC adjudication of a fraud claim arising from the same transaction should offend no one's notion of sound

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[7] 17 C.F.R. §12.23(b)(2) provides in its entirety: *Counterclaims*. An answer may set forth as a counterclaim facts alleging a violation and a request for a reparation award that would be a proper subject for a complaint under §12.21 or any claim which at the time the complaint is served the registrant has against the complainant if it arises out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint.

public policy. At any rate, it is *Congress'* notion of sound public policy that must prevail, and Congress, in enacting CEA section 14, perceived the CFTC's expertise as necessary to effective adjudication of complaints alleging violations of the CEA by registered persons. There is no evidence of a similar Congressional perception with respect to breach of contract complaints.

Separate administrative adjudication of section 4b fraud violations does not bring about any inefficient or inequitable fragmentation of federal court litigation. Rather, it logically results from Congress' desire to bring before one government agency, possessing ample adjudicatory and discovery powers (*see* PB 12-13, n. 26) all allegations of CEA violations committed by registered persons. *Amici's* ideas of efficient court procedures should not be allowed to frustrate Congress' purpose nor modify Congress' enactment. The exclusivity of an administrative forum for CEA litigation resulted from a deliberate, exhaustively debated legislative decision which should not be subverted by means of judicial creation of a private cause of action for fraud.

CONCLUSION

For the foregoing reasons, as well as for those raised in Petitioner's Brief, the decision of the Court of Appeals with respect to a private right of action for fraud under the CEA should be reversed.

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